

**PROTECTION OF EMPLOYEE RIGHTS UNDER CONTRACT-
ING OUT PROCEDURES AT THE NAVAL WEAPONS
CENTER, CHINA LAKE, CALIFORNIA**

HEARING
BEFORE THE
SUBCOMMITTEE ON CIVIL SERVICE,
POST OFFICE, AND GENERAL SERVICES
OF THE
COMMITTEE ON
GOVERNMENTAL AFFAIRS
UNITED STATES SENATE
NINETY-SEVENTH CONGRESS
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DECEMBER 13, 1982

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PROTECTION OF EMPLOYEE RIGHTS UNDER CONTRACTING OUT PROCEDURES AT THE NAVAL WEAPONS CENTER, CHINA LAKE, CALIFORNIA

MONDAY, DECEMBER 13, 1982

U.S. SENATE,
SUBCOMMITTEE ON CIVIL SERVICE,
POST OFFICE, AND GENERAL SERVICES,
COMMITTEE ON GOVERNMENTAL AFFAIRS,
Washington, D.C.

The subcommittee met at 8:15 a.m., in room 1318, Dirksen Senate Office Building, Hon. Ted Stevens (chairman of the subcommittee) presiding.

Present: Senator Stevens.

Staff present: Wayne A. Schley, staff director; Jamie Cowen, chief counsel; Edwin S. Jayne, minority staff director; and Pat Halcomb, chief clerk.

OPENING STATEMENT OF SENATOR STEVENS

Senator STEVENS. Good morning. I am sorry we are late.

We are holding this hearing today to receive testimony on the appeals process used by the Department of the Navy in its contracting out procedures at the Naval Weapons Center, China Lake, Calif.

The initial review at NWC, China Lake, showed that work could be done at a lower cost to the Government, about \$2.8 million lower, by retaining civil service employees to perform certain functions. Pan Am World Services, Inc., the low bidder, filed an appeal alleging deficiencies in the NWC cost estimate. An appeals officer from the Naval Material Command in Washington, D.C., was appointed to review the appeal.

The appeals officer, after reviewing the appeal by Pan Am, found in Pan Am's favor, stating that Pan Am could do the work for \$365,000 less than civil service employees. Employees and employee organizations then had the right to appeal the decision by the appeals officer.

The employees' appeal went to the same appeals officer, who again found in favor of Pan Am. While no one questions the integrity of the appeals officer, a Navy captain, there have been legitimate questions about the objectivity of an individual who made the original decision.

Of even greater concern is that the appeals process could not reconsider an issue previously raised by Pan Am. This denied to the em-

ployees the right to question any of the cost items. This also denied to the taxpayers the benefit of possible savings resulting from increased operational efficiency at an extremely important military facility.

The decision to contract but Government jobs is very significant. It impacts both the jobs of our civil service employees and the cost-effective performance of the Government. It is imperative that decisions be made with all the facts and that employees have the full opportunity to question the decisions in the process.

There continue to be questions about the RIF costs charged to the contractor, which would change the appeals officer's decision. It is possible that a more open and complete appeals process would have resolved these issues earlier.

I hope we can learn today why this questionable appeals process was used and if a more equitable process would have more fairly resolved the question of contracting out Government jobs in this case.

A larger question is, of course, whether changes in the appeals process, as indicated by this case, are necessary and if so, whether they should be done by legislation or administratively.

I am sorry that my colleagues, Senator Cranston and Senator Hayakawa, as well as Congressman Bill Thomas of the 18th district, could not be here. I know they are keenly interested in the subject of this hearing. On their behalf, I am submitting statements for the record.

[The statements referred to follow:]

STATEMENT OF SENATOR ALAN CRANSTON

Mr. Chairman, I am delighted that you are holding hearings on the issue of contracting out certain maintenance and supply operations at the Naval Weapons Center at China Lake, California. There have been a number of serious irregularities throughout the entire contracting process that concern me very much. I am pleased that this subcommittee has chosen to examine these irregularities. If we are to cut government costs and be fair to government employees, we must uphold the integrity of the contracting out process. The integrity of the process has been called into question because of the irregularities at China Lake.

Severe disagreements remain between the Navy, the General Accounting Office, and the Office of Management and Budget regarding the procedures used to determine the true cost to the government of contracting out these functions. As long as these disagreements exist, we cannot be sure that we've been fair to either the employees or the U.S. Government in the award of this contract. The basic rationale behind contracting out any government activity rests on finding that it would be cheaper to have the private sector perform the function than the government. Without demonstrating any savings to the government, there is no rationale for contracting out. The Navy has not demonstrated that real savings exist for this contract.

Specific guidelines have been developed over the years to ensure that the U.S. Government would have the most accurate assessment possible of the true costs of contracting out. These guidelines have not been followed in conducting the cost study for China Lake. The most glaring example involves the determination of the reduction-in-force cost to the government of converting to contractor operations. It appears that the Navy's methods significantly underestimated the true cost to the U.S. Government of reorganizing the functions under study for contracting out.

Another major concern of mine is that the Navy did not allow the employees at China Lake due process. The employees were in effect allowed only one appeal in two parts. The Navy determined that issues raised in the first appeal were nonreviewable in the so-called second appeal. In appointing the same review official for both parts of the appeal, the Navy did not take into account the possibility of human error or misjudgment. Again, the Navy did not act to find the true cost to the U.S. Government, and it did not act fairly to the federal employees.

Mr. Chairman, at best, it is uncertain that contracting out at China Lake Naval Weapons Center in this case will save the government money. In fact, the evidence is very strong that contracting out in this instance will cost the government considerably more than retaining the functions in-house. If the Navy awards this contract without resolving the outstanding issues and without determining the true cost to the government, the Navy will do a tremendous injustice to the federal employees at the Center and to the contracting out process. For the Navy to award this contract now would clearly violate Administration guidelines, as expressed in Circular A-76, as well as the intent of the Administration and the Congress to cut government costs and preserve the rights of federal employees.

I hope that the Secretary of the Navy will postpone this contract award until he can certify to the Congress that contracting out these functions at China Lake NWC will save the government money. I also hope that the Secretary of the Navy will issue a detailed written response to GAO's report on this matter, and that GAO has the opportunity to respond further to the Navy in writing before this contract is awarded.

STATEMENT OF SENATOR S. I. HAYAKAWA

Mr. Chairman, I wish to thank everyone, who on such short notice was able to attend this morning's hearing. I apologize that I am not personally able to attend, but I want everyone involved to know of my deep concern for the situation at China Lake. I believe this hearing is necessary not only to address the issue of contracting-out but for additional assurance that the Federal government will maintain a very clear policy when conducting cost-comparison studies.

To begin, I must make perfectly clear my position on contracting-out. I strongly support the free enterprise system and this government's reliance on it. It is not the business of the Federal government to be in business. If the private sector can perform commercial or industrial activities at lower costs to the federal government, then the private sector should be doing it. I have worked very hard in attempting to establish as a matter of policy throughout the government that private industry should be used to supply goods and services whenever that is practical, proper and cost efficient. As Chairman of the Subcommittee on Advocacy and the Future of Small Business of the Committee on Small Business I have been particularly concerned with what extent the Federal Government competes with private business, especially small business. Thus, if I am predispositioned in one direction, it is on the side of contracting-out, not retaining services in-house at an ultimate cost to the American tax-payer.

Last September, when the situation at China Lake was brought to my attention, Naval Weapons Center personnel had been informed that upon appeal by Pan American World Services, a decision to retain work in-house had been reversed. The cost-difference had swung in favor of Pan American by \$364,342. Nearly 200 civil service positions at China Lake were to be abolished. Because of my deep concern about the total effect on the Federal government when conducting nearly 200 RIF's, I wrote to Secretary Lehman and asked for a complete justification for the reversal of the contract award as a result of the appeal. Late last Friday I received a response to my inquiry. Hardly sufficient time to adequately arrive at a complete understanding of the Department's decision.

I am most distressed that this situation has escalated to the point that it has. The careers and futures of many Californians are at stake here. Further uncertainty has been added to the Navy's decision by the General Accounting Office. They have just completed a review of the Navy's procedures cost-comparison studies. I have had the opportunity to examine this report and would appreciate clarification from the Department of the Navy on the concerns which GAO raised. In particular, I am concerned about the method in which Naval Material Command (NAVMAT) calculated RIF costs in conjunction with reaching its most efficient organization (MEO) staffing level. In addition, it would then be appropriate and fair for the NWC employees to have adequate opportunity to respond to the Department of the Navy's clarification. Because of the serious implications which this contract award will have on the lives of many Californians and because of my continuing commitment that the integrity of the contracting-out policies of this Administration not be jeopardized, I request the Department of Navy to respond to the questions raised in the December 3, 1982 report from the General Accounting Office.

Again, I want to make it perfectly clear that I firmly believe that it is the function of the private enterprise system to provide goods and services needed to manage Federal programs. And it is this belief which compels me to be certain that this policy is not being undermined by any prefashioned conclusions. I do not believe that it would be in the best interests of contracting-out policies to award any contract when the practicality and cost-efficiency of the award is being seriously questioned by the General Accounting Office.

Thank you, Mr. Chairman.

STATEMENT OF CONGRESSMAN WILLIAM M. THOMAS

Mr. Chairman, I wish to thank you and the members of this Subcommittee for the opportunity to testify before your Subcommittee on Civil Services on the problem of the appeals rights of the employees at the China Lake Naval Weapons Center in Ridgecrest, California who would be affected by a decision to contract out 203 family housing, supply and warehousing operations, vehicle operations and maintenance positions.

Briefly, the background of the case is this. The original estimate by the Naval Weapons Center for in-house performance of these jobs was \$2,800,000 less than Pan Am's and it was announced that NWC personnel had been awarded the contract. On appeal by Pan Am, the Naval Material Command on August 27 reversed the earlier decision to retain this work in-house. During this review of Pan Am's appeal, the Naval Material Command increased the cost estimate of the in-house bid by \$1,320,000 and reduced the estimated cost of contracting out by \$1,850,000 making the contractor's bid the lower by \$364,342.

Four hundred and twenty-one potentially affected individuals appealed the decision. And it is to certain peculiarities in this appeals process that I would like to call the Subcommittee's attention. First, the same official who had heard Pan Am's appeal now heard the challenge to that appeal raised by the employees of China Lake. Thus the reviewing official was placed in the position of passing judgment on his earlier decision. Second, under the ground rules of the Navy's appeals process the only issues which could be raised during the second round of appeals were issues which had not been previously addressed. This set of procedures could deny parties to the case a fair hearing, and the potential exists for the manipulation of these ground rules by adversaries in the process.

Finally, I wish to comment on the substantive issues which have been the subject of this appeals process.

It is my understanding that OMB A-76 guidelines require that the cost of a RIF in eliminating positions be charged to the contractor. The number in this case is 203. The Naval Weapons Center in its original bid charged the contractor for a RIF of 207 positions. Based on OMB guidelines, it seems to me that this was inappropriate for the Naval Weapons Center to do since the cost of reaching the most efficient organization cannot be charged to either party. The correct number should have been 203. However, the Naval Material Command in its appeals decision started with 191 positions, and then said that 40 positions were common cost and charged only 151 to the contractor. Why did the Naval Material Command delete the RIF costs charged to the contractor by 40 positions when OMB guidelines clearly state that the cost to reach the most efficient organization are not to be included in the cost comparison? What is the RIF cost and its effect on the bids if the contractor is charged with RIF costs of 203 positions or even 191, as opposed to the 151 figure used by Naval Material Command?

It is my hope that the Subcommittee will see fit to address the deficiencies which currently exist in the appeal's process established by the Navy for the resolution of contracting-out disputes. It is also my hope that the Navy will seek to resolve the substantive issues which still remain over this particular case before proceeding with the contract award.

Senator STEVENS. This is an odd time to hold a hearing, early on a Monday morning, but it is a busy week, and I know there is a short timeframe for the review of this matter.

Our first witness is Chapman B. Cox, Deputy Assistant Secretary for Logistics, Department of the Navy.

I know you are married to an Alaskan, so you can't be all bad.

Mr. Cox. We have that in common, and also our law school in common.

TESTIMONY OF CHAPMAN B. COX, DEPUTY ASSISTANT SECRETARY OF THE NAVY FOR LOGISTICS, ACCOMPANIED BY GEORGE A. SAWYER, ASSISTANT SECRETARY OF THE NAVY FOR SHIPBUILDING AND LOGISTICS; CAPTAIN ZEANIOUS "ZEKE" NEWCOMB, DEPUTY DIRECTOR, NAVY LABORATORIES, USN; AND THOMAS NEUBERGER, BRANCH HEAD, NAVAL LABORATORY OPERATIONS DIVISION, USN

Mr. Cox. It is a privilege to be here this morning and I am the one in the Navy at my level with cognizance over installation and facilities, and that includes contracting out procedures which we are engaged in.

Also sitting at the table is my superior, Mr. George Sawyer, Assistant Secretary of the Navy. He is the Navy's acquisition and procurement executive.

We believe it is incumbent on this administration to manage the business of the Defense establishment as efficiently as possible. As we request large amounts of defense appropriations, not only must we express our resolve faithfully to administer the taxpayers' trust, we must also demonstrate that we are achieving maximum performance with their dollars which we are spending.

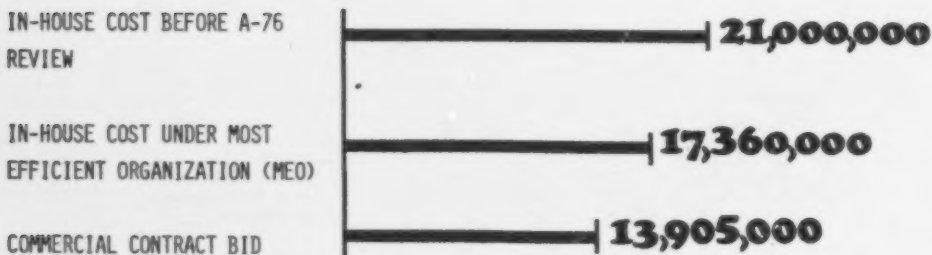
One means of achieving substantial savings is regularly to study all of our commercial and industrial operations to determine how they can most efficiently be performed. OMB Circular A-76 describes the process used to accomplish this review.

An A-76 study was conducted on certain housing maintenance, supply, and vehicle operations and maintenance functions at the Naval Weapons Center, China Lake, Calif. This review and subsequently solicitation of commercial bids revealed that the estimated cost of in-house performance exceeded \$21 million; that the estimated cost of in-house performance based on the most efficient in-house organization [MEO] would be \$17.4 million; and that the commercial contractor's bid price to perform the same work is \$13.9 million. This is exhibit I.

[Exhibit I follows:]

EXHIBIT I

**Basic Costs Revealed
by A-76 Study**



Mr. Cox. A-76 requires that in order to compare the in-house and commercial costs fairly, certain adjustments must be made to the commercial contractor's bid. First, a maximum adjustment of 6 percent of the bid must be added to account for the Government's costs of administering the contract. This amounts to \$834,000.

Second, one-time changeover costs of \$627,000 were added to the contractor's bid. This adjustment consists of several cost elements influenced by many variable factors, some of which are subject to dispute. The adjustment in the stated amount was determined to be appropriate based on the information available to the Reviewing Officer at the conclusion of a two-step appeal. The amount of the adjustment is still believed to be reasonable.

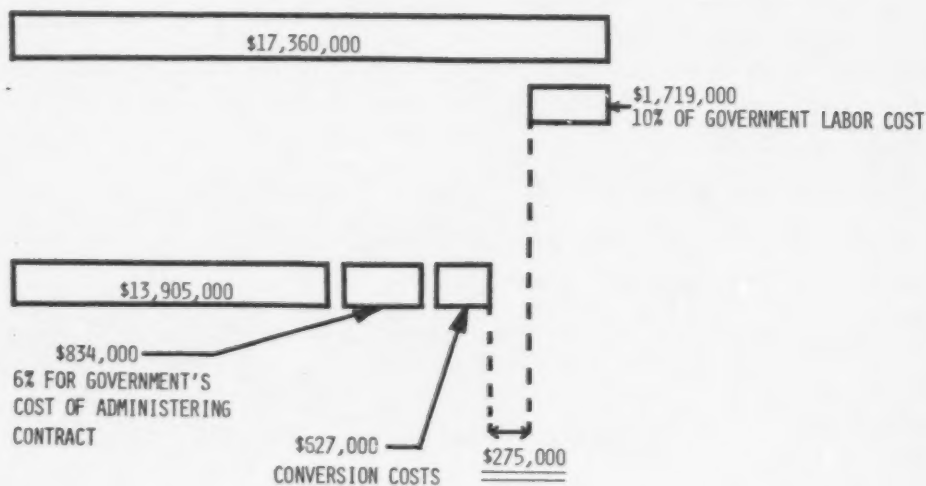
Finally, because the study represents an estimate of costs which cannot be precise, the contracting cost is required to be below the in-house cost by 10 percent of the Government's labor costs before a changeover is approved.

As you can see from exhibit II, after these adjustments were made, contracting out was favored by \$275,000. In view of this and the fact that the total in-house cost exceeds the contracting cost by almost \$2 million, a decision was made to contract out.

[Exhibit II follows:]

EXHIBIT II

Cost Comparison of In-House and Commercial Costs



Mr. Cox. Since many of the adjustments and costs are based on estimates, the actual savings could be slightly more or slightly less than \$2 million. While there may be some temporary loss in productivity during the changeover, there may also be a similar loss in implementing the most efficient Government organization if the function remained in-house. These unquantifiable costs are relatively small and tend to balance out.

We believe that the actual savings at NWC will approximate \$20 million for the 3-year study period. The Navy is proceeding with the contract conversion and, in the meantime, staffing has been reduced through attrition in anticipation of this event.

The A-76 appeal process was designed to adequately and fairly protect the interests of all affected parties without causing undue obstacles in carrying out the decision. Under A-76, only one appeal is required to address issues related to the cost comparison, but the Navy in an abundance of caution, uses a two-step review process. Any interested party may appeal.

In the first step, the appellant delivers a written statement of the grounds of his appeal. A reviewing official is appointed and it is his responsibility to obtain and review all the facts and regulations related to each item of appeal. He does not base his decision solely on information presented by the appellant.

In this case, the cost analysis team at NWC submitted detailed, comprehensive response to each item in the contractor's appeal. The appeal investigation is often conducted by an appeal team, which was the situation at NWC.

The appeal team and reviewing official made every effort to provide a proper accounting of costs and to fairly represent the interests of all affected parties whether they file an appeal or not.

At NWC, for example, about half the total adjustment asserted in the contractor's appeal was denied by the reviewing official. In reaching decisions on individual appeal items, all appropriate data was collected by the appeal team and the decisions made were fair.

In the first step of the appeal, the reviewing official only reviewed issues raised by the contractor because the contractor was the only party who complained. As a safeguard, the second step of Navy's appeal process offered the affected employees an opportunity to identify additional issues. At NWC, the employees and unions identified 12 new issues, two of which were determined to be valid and monetary adjustments were made to the cost comparison.

The most significant issue remaining in dispute is referred to in Senator Stevens' letter to Mr. Sawyer, dated December 8, 1982; namely, how properly to account for the costs of the Government reduction in force.

[The letter referred to follows:]

U.S. SENATE,
 COMMITTEE ON GOVERNMENTAL AFFAIRS,
 SUBCOMMITTEE ON CIVIL SERVICE, POST OFFICE,
 AND GENERAL SERVICES,
 Washington, D.C., December 8, 1982.

Mr. GEORGE A. SAWYER,
*Assistant Secretary of the Navy for Shipbuilding and Logistics, U.S. Department
 of the Navy, Washington, D.C.*

DEAR MR. SAWYER: Thank you for your letter of December 3. Unfortunately, it does not clear up the central question—will your actions in China Lake actually save the federal government money? I am not convinced that it will. In fact, the evidence seems to point to the opposite.

For example, the OMB letter states that it is correct that the reorganization costs to get to the most efficient organization should be normal government costs and should not be included in the cost comparison. OMB states the only reorganization costs that should be included (as a charge to the contractor) are the estimated reorganization costs (RIF costs) of going from the MEO to no organization in preparation for contract operation. The number of positions at the Naval Weapons Center at China Lake for the most efficient organization is 203.

I have received the mock RIF sheet from the NAVMAT appeal decision. Based on the above OMB position, you are correct that the initial RIF included 207 positions rather than 203 and therefore overcharged the contractor for the RIF costs of 4 additional positions. My review of the sheet shows that the appeal decision used the number of 191 rather than 203 positions to start. The appeal decision further reduced the number of positions by 40 MEO excess and MEO downgraded positions. The result was to undercharge the contractor for the reorganization costs (RIF costs) by 52 positions.

Employees at China Lake claim that if the correct figure of 203 was used in calculating RIF costs, the contractor would be charged an additional \$688,807, or enough to continue the function in-house at a savings of over \$400,000. I am also informed that if the RIF occurs, 102 individuals will receive retained pay while NAVMAT in their appeal only costed for 23.

I would appreciate knowing how the cost savings by contracting out would be affected if the contractor is charged for RIF costs for 203 positions rather than 151. I would also appreciate knowing what rationale NAVMAT used in costing only 151 (190 minus 40) positions rather than 203, in light of OMB's policy.

According to your letter, the second step in the appeals process was instituted only to review issues concerning the original cost comparison that were previously unknown or not revealed at the time of the first appeals proceeding. By limiting the second appeal to only those issues not revealed during the first appeals proceeding, those individuals who were not party to the first appeal (employees and employee organizations who believed the in-house bid had won) have been effectively frozen out of the appeals process. These individuals cannot join issue with the contractor's appeal or the decision to support those appeals issues.

As can be shown by our exchange of letters, there are many who believe that the appeals officer erred in his appeal decision, but employees and employee organizations have not been allowed to address those issues directly with the appeals officer.

With best wishes,
 Cordially,

TED STEVENS, *Chairman.*

Enclosure.

P.S. I feel it is important that federal employees be given the right to appeal all those areas in question. Or, suspend all action pending a hearing by my Subcommittee at 8:00 a.m. on Monday, December 13.

ADJUSTMENT OF MOCK RIF BASISORIGINAL NWC BASIS

207	FTP Positions Abolished
154	Separations with Severance Pay
53	Separations without Severance Pay
61	Downgraded with Retained Pay

REVISED BASIS USED IN THE APPEALS REVIEW

191	Actual On Board FTP Positions as of 07/31/82
- 9	MEO Excess Positions Treated as Common Cost
182	Net FTP Positions Abolished
135	Net Separations with Severance Pay (Prorated)
47	Separations without Severance Pay (Prorated)
54	Downgraded with Retained Pay (Prorated)
- 31	MEO Downgraded Positions Treated as Common Cost
23	Net Downgraded Positions to be Costed

NOTE: At least 20 of the original 61 downgraded employees are eligible to retire immediately. A high number of these employees can be expected to retire and accept employment with the contractor at a substantial net increase in income. Average minimum DOL wage rates paid by the contractor exceeds the average rate paid by NWC.

Items 14.a, 14.b, 14.c,
14.f and 14.h

ATTACHMENT A

BEST COPY AVAILABLE

Mr. Cox. NWC's original estimate of RIF costs had not forecast any attrition, vacancies, retirements or other factors that would reduce RIF costs. At the time of the appeal review, there were only 191 employees subject to the reduction in force. The other 12 positions required in the MEO were either vacant or filled by temporary employees that would incur no RIF costs.

Of the 191 permanent employees on board as of the appeal, 9 still did not fit in the MEO and 31 required grade reductions. The reviewing officer appropriately adjusted for that portion of the RIF costs relating to these 40 employees which had been unfairly charged against the contractor.

The manner in which this adjustment was made also compensated for attrition, vacancies, retirements, and other factors which previously had not been properly taken into account.

We appreciate that there are additional questions by the Congress and will attempt to answer these questions. Award of the contract and issuance of RIF notices have been suspended for this hearing.

We have reexamined our decision. We consider it to be proper and the contracting out at NWC to be cost effective.

Thank you, sir.

Senator STEVENS. Thank you, Mr. Cox.

Captain Newcomb, do you have a statement?

Captain NEWCOMB. No, sir.

Senator STEVENS. Mr. Sawyer.

Mr. SAWYER. No, sir.

Senator STEVENS. Mr. Neuberger.

Mr. NEUBERGER. No, sir.

Senator STEVENS. Let me tell you my interest here. I have seen so many times in contracting out up my way that on the first go-round, it is very advantageous to the Government to contract out to commercial firms functions normally performed by Federal employees. But as soon as the civil service group is disbanded, as soon as there is no one to compete with the commercial firm, the cost to the Government shoots up.

In one case, a contract out of Atlanta, twice annual round trip expenses for the employees were cranked in, but that was never figured into the original bid.

I just read an article over the weekend that criticized the Government for contracting out. We see time after time that it is not in the best interest of the Government to disband the civilian work force unless there is competition in the affected area for the kind of work to be performed, and unless there is a very fair comparison.

With regard to the job you just mentioned, you have an ongoing RIF now, and that RIF apparently is proceeding according to normal Government procedures. Why the comparison to the mock RIF rather than the most efficient operation personnel level?

Didn't you compare the actual reduced force to the bid of the contract instead of the mock RIF?

Mr. Cox. Sir, that is what we are doing. We were using the 191 as opposed to the 203, which was constructed in the beginning.

There were attritions that occurred between the time that the original computations were made and the time that the appeal process took place, and there have been, in fact, further attritions since that time.

Senator STEVENS. The figures are the mock RIF's, not the actual RIF's.

Captain NEWCOMB. I believe you have reference to the fact when it came time to actually issue RIF notices, the management updated their data and computed a new information. Some people out there are referring to this as the actual RIF in that it identifies the employees who must be given RIF notices.

But I will point out to you, sir, that the actual cost of the RIF will not be known probably until the end of the contract period because of such things as: after these RIF notices go out, individual employees must make their own decision about whether to bump someone else, whether to go to work for the contractor, or retire, if eligible, et cetera. We also make an effort to relocate them in other governmental activities.

Until all these decisions are actually made, one cannot compute what can be referred to as "actual and true RIF costs."

Senator STEVENS. Well, that brings up the avenue of your appeal. As I understand it, the employees were not permitted to raise before the contracting officer the issue pertaining to the actual RIF costs because that was raised before by Pan Am on their appeal. Is that right?

Mr. Cox. Sir, what happens on the appeal is that anybody can raise an issue on an appeal. This is not a hearing where parties come in and argue their case. It is the management's responsibility to represent the interests of all affected parties in the appeal process.

It is not really an appeal like you would conceive an appeal in court—

Senator STEVENS. I have handled these before the Navy, 30 years ago, but I don't think they have changed much since then.

Mr. Cox. In this case, the review team looked into those issues carefully, collected data, made decisions we think appropriate and fair and those issues were decided.

After the first appeal was offered, other issues were raised by the employees and we looked into those. I think just the decision itself is indicative that the reviewing officer was not one-sided. In this case, when he rejected two times as many claims made by the contractor as he granted.

Senator STEVENS. Well, I am informed that the contracting officer denied the employees the right to question any of the cost items because they had in fact been questioned by Pan Am on the first appeal.

Mr. Cox. Well, I think that is a misunderstanding of the process.

The contracting officer looked into those issues very carefully on behalf of the employees during the first appeal, and to raise the issues again was just raising an issue he had already reviewed and decided upon.

Senator STEVENS. Mr. Cox, these issues are being raised from a different point of view. On the second appeal, Pan Am won and reversed the original Government decision which was, as I understand it, that there should be no contracting out. It was not to the advantage of the Government.

Am I wrong?

Mr. Cox. That was the adjustment made by China Lake.

Senator STEVENS. So the contracting officer says on review of Pan Am's appeal that this is wrong.

Mr. Cox. He didn't just look at Pan Am's appeal, he looked at all the facts and took into account the concerns of the employees. He asked NWC for input and they gave a response to every complaint.

Senator STEVENS. Are you saying that the employees and employees' organizations were present at the time of the first appeal?

Mr. Cox. Nobody was present, then.

Senator STEVENS. They had representations?

Mr. Cox. They had no representations. The contracting officer did this in his review of the administrative process. There was no hearing.

Captain NEWCOMB. Let me clarify this—

Senator STEVENS. Sir, let me ask you this: Is Pan Am organized by labor unions?

Captain NEWCOMB. I don't know. I have heard statements made that it is not, but I really don't know.

Senator STEVENS. Did the contracting officer have any union organization before him at the time he challenged the original finding by the Government?

Captain NEWCOMB. I want to clarify two points: I am an appeals officer, and I clarify that because there is a contracting officer and he has a different function and I don't want to confuse anyone by mixing the two.

Senator STEVENS. You are the appeals officer. I beg your pardon, I thought you were the same thing. They appeal to the contracting officers. But you are an appeals officer?

Captain NEWCOMB. Yes, sir.

Let me explain this. The appeals were submitted in writing. There was no hearing as Mr. Cox explained. The appeals were made in writing; as he explained, and prior to August of this year, there was only one opportunity for anybody to appeal and that was immediately following the bid opening and at that point, anyone, any interested party had the right to appeal.

In this case, the contractor was the only party to submit an appeal, his appeal was made available to the people at China Lake, and they used that to prepare, for my use, statements of their position on all the issues in the appeal.

Before any decision, my team went out to China Lake and collected data. But I want to emphasize that once an issue such as the RIF was raised by the contractor, I did not simply look at the things he criticized about the RIF, but the entire RIF calculation and I assessed from the point of view of both the Government, the employees, and the contractor, and tried to arrive at a position that was fair to all parties.

Senator STEVENS. You heard the first appeal from Pan Am, right?

Captain NEWCOMB. I reviewed it, sir, is more correct.

Senator STEVENS. Now, when the second appeal comes up, the people who are grieved by the first decision appeal come to you, too. Is that right?

Captain NEWCOMB. That is correct, and I think the rationale for this is because the rules say that once a decision is made on a particular issue, that issue cannot be raised again, and since all the issues were

new and not issues I had ruled on before, it seems fair to allow the same appeals officer to review those also.

I am sure you understand it takes a lot of homework to get oneself in a position to review and make a decision about them.

Senator STEVENS. I understand that.

Captain NEWCOMB. Once somebody did that, there—

Senator STEVENS. But did you have the actual RIF before you at the time you decided the Pan Am case?

Captain NEWCOMB. Again, I will emphasize, sir, we have confused what is termed an actual RIF with an actual RIF. There are such things you compute for the RIF, such as you compute—you try to estimate—how many people are going to be in a retained pay status.

You also have to estimate how long they will remain in that status. They get out of that status by finding other jobs or being promoted or becoming eligible for retirement, and you never know how long they will be there until it happens.

So this contract will be completed before we can probably give you an accurate figure of precisely the RIF cost.

Senator STEVENS. You reduced the number of people involved by 40, I am told?

Mr. Cox. Yes, sir.

Senator STEVENS. The result of that was what gave the advantage or the numerical computation showing there was an advantage on the side of Pan Am?

Captain NEWCOMB. That was one of the factors.

Now, I think it is important that we understand in addition to all the complexities in the RIF process itself, it was further complicated in this situation because the management at China Lake constructed a most efficient organization which was significantly different from what was presently on board at the time performing these functions, and this gave us a situation in which the MEO involves fewer employees and positions of lower pay than what was on board, and, yet, when they computed RIF costs to the assessed, the contractor for the cost for converting to that, they used the on-board count.

When they computed the cost of doing business in-house, they used the MEO.

Mr. Cox. Let me try to answer the 40 people question, sir, but first, I want to emphasize what Captain Newcomb said, and that is actual RIF costs are different from RIF notices and we cannot confuse that. That is what we were trying to get to in the review process, trying to figure out what would be the most reasonable estimate of actual RIF costs, because we think that is the fair thing that should be used to adjust. Let me just answer the 40 for you, if I can.

The 40 people consist of two groups. One is nine people who cannot fit into the most efficient organization. For those nine people, their RIF costs are, under the laws and regulations, not chargeable to the contractor.

The other 31 people, in order to get into the most efficient organization situation, would have had to be downgraded. Under the regulations and rules, the cost of downgrading those people in the most efficient organization are clearly not chargeable against the contractor.

So any retained pay relating to downgrading those 31 employees are not chargeable against the contract.

Now there may be some additional downgrading of those 31 people as a result of going from the most efficient organization to going into the contractor's status. But those costs—that portion of their retained pay which would relate to that small additional downgrading—was determined to be overbalanced or at least equalized by any additional anticipated attrition, retirements during the bumping process, or those who might go to work for the contractor which was not previously taken into account.

Senator STEVENS. But I don't understand how you can conclude that there are nine positions that are treated as common cost. Perhaps I can understand changing from 207 to 191, but you have a total of 40 here that are treated as common cost.

Now, I don't see how they are common cost when Pan Am never had them on board. How can they be common cost to Pan Am when they are Government employees, and apparently were intended to be downgraded as a cost savings mechanism to present the contracting out.

Mr. Cox. Under the rules, it is a common cost if the Government would have to bear the cost anyway to get to the MEO, and that is the reason that it should not be charged against the contract.

Captain NEWCOMB. It is common cost in the sense that it would be experienced whether you were going to MEO or to a total RIF. It is common to both evolutions.

Senator STEVENS. Maybe I am wrong, but I see some out there who have in their mind that Pan Am has a chance to win a contract, so he undertakes to trim down his operation as far as Government employees are concerned at a cost savings to the Government automatically.

Then having instituted that on appeal, that unit is in worse shape than if they had not tried to save money, if they had kept the 40 people on board and not indicated any RIF at all, you would have used as a minimum 203. 207 was the actual number, but they started some RIF's, started some reduction in force to save the Government money and you end up by taking the cart away from them. I don't understand that.

Mr. Cox. No, sir, when we say we are down to 191 on the first of August and 176 on October 1, we are talking about people subject to RIF.

We have not sent them away, we have hired people on temporary status to do the job. We have not sent people home. Just as we get attrition, we are taking care of it in ways that won't escalate our RIF costs and I think that is good practice.

Mr. NEUBERGER. Sir, the adjustment related to the 40 positions is well under \$1 million. The savings in their MEO was about \$4 million, so clearly by getting more efficient, it was advantageous to themselves—

Senator STEVENS. Sir, was there any competition in the bid? Is Pan Am the only one who sought this business?

Captain NEWCOMB. No, there were two or three other contractors—I believe three.

Senator STEVENS. Does China Lake already have some contracting out?

Captain NEWCOMB. Yes, sir.

Mr. NEUBERGER. There were no contract conversions at China Lake. They have some ongoing contracts that they had for—

Captain NEWCOMB. They had a number of functions out on contract which were recently combined into a single contract, but these were not done through this same process is what Mr. Neuberger is saying.

Senator STEVENS. I am informed that the GAO report says the Navy is wrong. If you follow OMB results, what is the cost of your decision?

Captain NEWCOMB. In that case, we did not do what was contained in the GAO report. A misunderstanding occurred because they—GAO—asked OMB a question which they answered straight-forwardly, but the question implied conclusions that were erroneous. When a true situation was explained to OMB, they said the procedures we used were correct.

Mr. Cox. We have a letter that we will submit for the record.¹

Senator STEVENS. I would like to have it, but I asked what is the comparison if you use 203. Maybe you can discuss it with OMB, because I am told they said 203 is the figure that should have been used for RIF costs for employees.

Captain NEWCOMB. As I explained earlier—

Senator STEVENS. Captain, can you answer the question? Did you compute it on the basis of 203 or not?

Captain NEWCOMB. No, sir.

Senator STEVENS. Wasn't that the OMB direction to you at that time?

Captain NEWCOMB. No, sir, and I will be glad to explain it.

Senator STEVENS. You can go ahead and explain it, because I don't understand it.

Captain NEWCOMB. The situation I mentioned earlier is that OMB did not anticipate an MEO significantly different from the onboard count, so they didn't specify if we should use onboard organization or the MEO to do a mock RIF. GAO asked what the procedure was, and they said use MEO, but when it was explained to them we had a situation in which the onboard organization contained people of significantly higher pay grades, they agreed that the contractor should not be penalized for downgrading those employees to the right pay grade.

Senator STEVENS. Why is that the case? If you have procedures in the Navy to allow people in civil service to work a number of years to get higher pay grades, then if you are not going to use those actual grades at the time of a challenge for contracting out, every challenge is going to win, because these people are entitled to in-grade pay raises and they are entitled after a period of time to the salary they are getting.

But you put together a mock that says no, those are more than normal and we won't count those.

Captain NEWCOMB. No, sir, I didn't put it together. The management at China Lake in company with representatives of the union agreed to it.

If you want to take what you suggested and we use the existing onboard organization for the RIF, then we should use that same organization in computing the cost of doing the work in-house.

¹ See p. 18.

All I am saying is it is not reasonable to use that organization to compute the cost in-house but use a larger, more expensive organization as the basis for computing RIF costs.

Mr. Cox. Sir, if we had not gotten down to that number, we would be comparing the \$21 million with the current level of employees. What we are saying, if you use MEO, you should not charge the Government for getting to the MEO.

Mr. NEUBERGER. Even if the Naval Weapons Center was at the MEO, and the cost of RIFing the same as in the MEO, we still would have had to make the adjustment in the RIF cost for a worse case mock RIF, and that is an adjustment that GAO agrees with. So the adjustment for 40 covers two points here and we still would not have used the original RIF cost, even if they were at MEO.

Senator STEVENS. The only thing that sticks in my mind is if you use this procedure, I don't see how any existing Government entity can withstand a contracting out challenge so long as the bid is lower than the mock RIF.

Captain NEWCOMB. Sir, I will point out, some of the other laboratory centers I am responsible for managing have indeed succeeded in the competition in-house—

Senator STEVENS. Does Pan Am have any other services on China Lake?

Captain NEWCOMB. Yes, sir, one other contract.

Senator STEVENS. What is that, do you know?

Mr. NEUBERGER. Guards, grounds keeping, janatorial, and services like that.

Senator STEVENS. I have been asked to ask a series of questions from the Senators from California. I am told Senator Cranston has asked to delay the letting of the contract until the Navy responds to the GAO.

Why can't you do that?

Mr. Cox. We have prepared our comments to the GAO report, and we can respond in writing. In terms of delaying the notices, we could delay the notice—if we gave a 60-day notice—for a few more weeks.

We wanted to give a 90-day notice and felt constrained to go ahead. We have talked to GAO and will be in a position to discuss it with them more.

Senator STEVENS. Does the Government have liability to Pan Am before it signs the contract?

Mr. Cox. Potentially.

Senator STEVENS. What?

Mr. Cox. Before it signs?

Senator STEVENS. Yes.

Mr. Cox. Has it signed the contract with Pan Am?

Captain NEWCOMB. No, sir, but we have a potential liability, because when we go out with a request for proposal, we state the conditions under which we intend to award a contract to the low bidder and if we back away from those conditions, we are potentially in danger of being accused of not acting in good faith.

Senator STEVENS. If the basis is that they are not the low bidders. I don't see how there could be liability for Pan Am, and that is why

I wonder what is the reason the Navy wouldn't give the time the representatives from California seek to have these reviewed.

Mr. Cox. Sir, we have been reviewing it since August and we think we have covered all these questions, and we have talked to GAO and we think they are satisfied with it.

Senator STEVENS. Well, the Representative from California wants to know also why 40 employees were omitted from the RIF cost. I think I understand what you are saying, but I don't understand why you are doing it. Why didn't you move to achieve the most efficient organization from the Weapons Center by cutting 40 employees from the contractor's RIF cost, too?

The company came in and looked and saw there were 207 employees, and said, "I can do it for X number of employees." The company said the model would be 40 less, and so that is what we will compare, thus giving us the advantage, because, as I understand it, these are to be treated as common costs. They were not common costs in his bid, was that not so?

Mr. Cox. They are treated as not being chargeable against the contractor, because they would have to be incurred by the Government, whether we win the contracting out or not.

Captain NEWCOMB. Sir—

Senator STEVENS. Now wait, that means if we find some way to direct you not to do this, that you would tell China Lake to operate the affected operation at 151 people, is that right?

Mr. Cox. No, sir, 203.

Senator STEVENS. How could it possibly be charged to the Government? Why is it a common cost?

Mr. Cox. The cost of retained pay to get down to 203 would have to be borne by the Government, sir.

Senator STEVENS. We are at 207. How do you have 40 numbers to get down to 203? It is just 4, not 40.

Mr. Cox. Yes, 203 is the most efficient organization.

Forty has to do with the people that have to be downgraded to get to 203.

Captain NEWCOMB. It is important to recognize that this most efficient organization does not just involve total number of employees to be used, it specifies particular skills and pay grades, and in this context that 40 comes up. In reference to what you said earlier about the contractor looking at the Government's organization, I should point out, what he saw in place were 253 people, about 207 full-time permanent, and 46 temporaries performed this function. He was not privileged to know what the Government structure for the most efficient organization was while he was preparing his bid. He did not have access to the Government's efficient organization until after bid opening.

Senator STEVENS. Let me ask this one question, Mr. Cox:

Are there RIF costs here in terms of severance pay that would not be charged against the cost of converting the contract or operations?

Mr. Cox. To the extent that they are in there for getting to the most efficient organization, they were taken out by the reviewing officer. They were not charged against the contractor, yes, sir.

Senator STEVENS. But their actual cost to the Government will incur—

Mr. Cox. They're actual costs which the Government incurs, no matter what we do. That is the reason they are not charged against the contract.

Senator STEVENS. But in order to get the most efficient cost operation, you would have to let go people who had higher pay brackets.

Mr. Cox. Yes, sir.

Mr. STEVENS. With more time and grade, with the Government longer.

Mr. Cox. To get with the most efficient organization, yes, sir.

Senator STEVENS. You are prepared, if the Government kept the contract in-house, to represent that these people be fired because they have longevity.

Captain NEWCOMB. They would not be fired, they would go through a bumping process.

Mr. Cox. That is retained pay, not getting rid of them. We are talking about the difference between what their higher pay would be in those downgraded positions and what it would be if there were new employees in there at lower pay grades.

Senator STEVENS. By definition you are not charging that against the contractors?

Mr. Cox. Because that is going to the most efficient organization.

Senator STEVENS. It seems to me you are giving them an advantage of the Government's desire for efficiency and the net result is that they be contracted out.

Mr. Cox. If you don't do that, sir, the logic would compel you to compare the bid to what the cost is now. You either compare the bid to the most efficient organization or to what it costs us now, and what it costs now is over \$21 million. That is clearly inefficient. So if you compare the contractors' bids fairly, then you should not charge the— if you are going to reduce the cost by \$4½ million, you should not charge the contractor with what it is going to cost you to get that \$4½ million reduction.

Senator STEVENS. All right, I thank you, gentlemen, and we will hear from the GAO. I have to get to another meeting.

There may be other questions that the Senators from California want to ask you.

Thank you very much, gentlemen.

[Letter to Senator Stevens from Mr. Cox, with attachments, and responses to questions submitted by Congressman William M. Thomas follow:]

DEPARTMENT OF THE NAVY,
OFFICE OF THE ASSISTANT SECRETARY,
(SHIPBUILDING AND LOGISTICS),
Washington, D.C., December 17, 1982.

HON. TED STEVENS,
Chairman, Subcommittee on Civil Service, Post Office and General Services,
Committee on Governmental Affairs, U.S. Senate, Washington, D.C.

DEAR MR. CHAIRMAN: Attached is the exchange of correspondence, to which I referred during the hearing on December 13, between Navy and OMB about the GAO report on contracting out at the Naval Weapons Center, China Lake, California.

If I can be of further help, please let me know.

Sincerely,

CHAPMAN B. COX,
Deputy Assistant Secretary (Logistics).

DEPARTMENT OF THE NAVY,
OFFICE OF THE CHIEF OF NAVAL OPERATIONS,
Washington, D.C., November 19, 1982.

Mr. DONALD E. SOWLE,
Administrator, Office of Federal Procurement Policy,
Washington, D.C.

DEAR MR. SOWLE: The enclosed letter report published by the General Accounting Office (GAO) on November 12, 1982 expresses reservations concerning the procedures used by the Navy during the conduct of the administrative appeal of the cost comparison involving base operation support at the Naval Weapons Center, China Lake CA (Solicitation No. 62474-82-R-0051). It implies concurrence by officials of the Office of Federal Procurement Policy (OFPP). We believe that the GAO may have misunderstood the actions taken by the Navy and, as a result, may have provided your staff with information misdirecting their judgment and conclusions.

We agree with the position taken by your staff that the cost of the reorganization to the most efficient organization should not be reflected in the cost comparison. In the comparison conducted at the Naval Weapons Center, however, the cost of this reorganization was included in the computation of the one-time costs of contracting.

The GAO report mistakenly assumes that the computation of one-time costs of contracting in the original comparison was based upon the most efficient organization. In fact these costs were based upon the existing organization which was considerably larger than the most efficient organization used in the computation of in-house costs. This situation resulted in the decision of the appeals officer to reduce the one-time costs of contracting by approximately \$1 million (the estimated cost to reach the most efficient organization).

I would appreciate your staff's reviewing the circumstances surrounding the actions taken by the Navy and providing us with a written opinion concerning their compliance with the policies contained in OMB Circular A-76.

Sincerely,

B. W. COOK,
CAPT, SC, USN.

EXECUTIVE OFFICE OF THE PRESIDENT,
OFFICE OF MANAGEMENT AND BUDGET,
Washington, D.C., November 22, 1982.

Captain B. W. COOK,
Office of the Chief of Naval Operations, OP-443,
Washington, D.C.

DEAR CAPTAIN COOK: This is in response to your November 19, 1982, letter to Don Sowle concerning General Accounting Office (GAO) Report B-209739 about the conduct of the Administrative appeal of Solicitation No. 62474-82-R-0051 at the Naval Weapons Center (NWC), China Lake.

The GAO report (page 4, paragraph 4) cites OFPP as stating that the reorganization cost to get to the most efficient organization (MEO) should be normal Government management costs and should not be included in the cost comparison. This is correct. The only reorganization cost that should be included (and then only to the cost of contracting) is the estimated reorganization cost of going from the MEO to "no" organization in preparation for contract operation.

Based on GAO's presentation of NWC's approach to computing one-time conversion costs, it appeared that the MEO was properly used as the basis for determining these costs. Since that approach is correct, it appears that no further adjustments should be made to these one-time costs by NAVMAT appeal officials. This resulted in GAO reporting that "OFPP did not know of any other instances where an agency had treated the cost of reorganizing to meet its MEO in the manner it was treated by NAVMAT." However, if the original computation of the one-time costs of contracting was based on the existing organization rather than the MEO, as your letter states, then the original NWC computations were inappropriate and must be adjusted to comply with current policy. Also, the GAO report (page 3, paragraph 2) states that the "mock RIF" was computed based on a worst case analysis; which, unless justified in unusual circumstances, is also inappropriate. The adjustments you said were made by the appeal officials to rectify these discrepancies are compatible with the cost comparison procedures in A-76.

The GAO report further states that reorganization costs would not be incurred if an activity is contracted (page 5, line 4). The one-time costs to get the organization to its most efficient level are theoretically incurred regardless of whether the function remains in-house or is contracted-out because this is the level from which the comparison to contract is made. These costs, as stated in the second paragraph above, are not added to either the in-house estimate or the cost of the contracting. Your letter indicates the appeal officials followed this guidance properly.

I hope these clarifications are beneficial. If we can be of further assistance, please contact us again.

Sincerely,

CURTICE E. HOLLAND,
*Deputy Associate Administrator
for Procurement Policy Development.*

RESPONSES OF MR. COX TO WRITTEN QUESTIONS SUBMITTED BY CONGRESSMAN
WILLIAM M. THOMAS

It is my understanding that OMB A-76 guidelines require that the cost of a RIF in eliminating positions be charged to the contractor. The number in this cost is 203. The Naval Weapons Center in its original bid charged the contractor for a RIF of 207 positions. Based on OMB guidelines, it seems to me that this was inappropriate for the Naval Weapons Center to do since the cost of reaching the most efficient organization cannot be charged to either party. The correct number should have been 203. However, the Naval Material Command in its appeals decision started with 191 positions, and then said that 40 positions were common cost and charged only 151 to the contractor.

Question 1. Why did the Naval Material Command delete the RIF costs charged to the contractor by 40 positions when OMB guidelines clearly state that the cost to reach the most efficient organization are not to be included in the cost comparison?

Question 2. What is the RIF cost and its effect on the bids if the contractor is charged with RIF costs of 203 positions or even 191, as opposed to the 151 figure used by Naval Material Command?

DEPARTMENT OF THE NAVY,
OFFICE OF THE SECRETARY,
Washington D.C., April 8, 1983.

HON. TED STEVENS,
*Chairman, Subcommittee on Civil Service, Post Office and General Services,
Committee on Governmental Affairs, U.S. Senate, Washington, D.C.*

DEAR MR. CHAIRMAN: This is in response to your letter of March 15, 1983, in which you asked for answers to two questions raised by Congressman Thomas in connection with your Subcommittee's hearing on December 13, 1982.

In answer to the first question, the estimation of reduction-in-force (RIF) costs at Naval Weapons Center (NWC), China Lake, was complicated by the fact that the staffing required by the Most Efficient Organization (MEO) structured by management was different from that on board prior to the study, in total numbers and especially in pay grades. When the Appeals Review Team examined the situation, the total number of permanent full time employees on board as of 31 July 1982 (191) was less than the number required by the MEO (203). However, nine of these 191 employees still could not be placed into the MEO because they did not have the right skills and thirty-one others would have required downgrading to match MEO pay grades. The Appeals Review Team used these forty positions as a basis for adjusting several inequities in NWC's estimation of RIF costs.

Costs associated with these forty positions would have been incurred in implementing the MEO if the functions had remained in-house. Therefore, fairness and regulations require that such costs be excluded from the RIF costs charged to the contractor. Also, no RIF costs were allowed to be charged to the contractor for the 12 positions (203 minus 191) which were vacant as of 31 July 1982.

In answer to the second question, the contractor was charged with the Naval Material Command's best estimate of actual RIF costs relating to the 203 positions. If the contractor had been charged with hypothetical RIF costs for the 203

positions based upon worst case scenarios without reference to actual circumstances or probable employee behavior and without excluding costs attributed to implementing the MEO, the adjustment to the contractor's bid would have been \$608,000 higher, making the Government's bid the low bid. Such a result would have been unrealistic, unfair and probably legally untenable.

I trust the information I've provided will be helpful. Your continued interest in and support of our programs are appreciated.

Sincerely,

CHAPMAN B. COX,

Deputy Assistant Secretary (Logistics).

Senator STEVENS. Next we have Mr. Robert Gilroy, Mr. Paul Jones, Mr. Harold Andrews, and Mr. Robert Stotts.

Do you have a statement?

Mr. GILROY. I do, Mr. Chairman.

TESTIMONY OF ROBERT M. GILROY, SENIOR ASSOCIATE DIRECTOR, PROCUREMENT, LOGISTICS AND READINESS DIVISION (PLRD), GENERAL ACCOUNTING OFFICE, ACCOMPANIED BY PAUL L. JONES, GROUP DIRECTOR, PLRD, GAO; HAROLD ANDREWS, SENIOR EVALUATOR, PLRD, GAO; AND ROBERT STOTTS, SENIOR EVALUATOR, LOS ANGELES REGIONAL OFFICE, GAO

Mr. GILROY. We are here at your request to discuss the results of work we performed at the request of Senators Alan Cranston and Paul S. Sarbanes relevant to the procedures used by the Naval Material Command appeals team in reversing an earlier decision made by the Naval Weapons Center (NWC) to perform various activities at the Naval Weapons Center, China Lake, in-house rather than by contract.¹ The activities the Navy intends to contract are family housing maintenance, supply operations and warehousing, and vehicle operations and maintenance.

As you are aware, Office of Management and Budget Circular A-76 generally requires a cost comparison to determine if it is less costly to perform an activity in-house or to contract. The circular also requires agencies to establish appeal procedures to resolve questions arising from determinations to either continue in-house performance or to contract out. Agency appeals decisions are final.

The Naval Weapons Center, China Lake, performed a cost comparison and determined it would be about \$2.8 million less over a 3-year period to perform the activities in-house than to contract. This decision was appealed by the contractor submitting the low bid and in the appeals process the previous decision was reversed because it was determined that the cost to perform the activities would be less costly by about \$364,000 if they were contracted.

Senators Cranston and Sarbanes posed specific questions to GAO regarding the appeals review and requested that we report to them before the Navy awarded the contract which was scheduled at that time for about November 15. Since we had approximately 2 weeks to answer the request, we looked primarily at areas involving large cost adjustments to the initial study, such as one-time conversion costs, escalation costs, and general and administrative expenses. In our November 12 response to the request questions, we found in summary that:

¹ See p. 25.

In regard to the question on why the Naval Audit Service did not identify the same discrepancies in NWC's in-house estimate that were found in the appeals process, we found that the items questioned in the appeals review reflected differences in judgment and interpretation while it was the responsibility of the auditors to determine mathematical accuracy and insure that NWC followed established procedures. Thus, it is doubtful, in our view, that the items questioned in the appeal would be identified in the auditors evaluation.

In answer to why the appeals review team did not consult naval personnel experts in performing their review, we found that they were only concerned about the number of hours and the number of people involved which, in their opinion, did not require personnel experts.

In response to the question on how the reduction in force (RIF) that would result from contracting was projected, we found that the appeals team adjusted the "mock RIF" to correct what was considered a "worst case" projection. NWC agreed that it should have used some other assumptions, but disagreed with the extent of the appeals team adjustment. We agreed that the worst case projection should not have been used.

In answer to the question of why the appeals team changed figures used to compute labor hours, we found the appeals team adjusted labor costs on the basis of actual hours in the 3-year contract period. We agreed that these adjustments were made accurate because of the use of actual work hours rather than a standard.

In response to the question of why the appeals rules were changed to prohibit a contractor from appealing elements reviewed in the first appeal, we found that Navy appeals rules were amended to allow appeals when a decision was reversed as the result of an initial appeal. However, the right of appeal was limited, not only to contractors but to any party, to questions concerning elements that were not considered in the first appeal.

The final question concerned the procedures used in the appeals process. While it appears that Navy followed the appeals procedures in its basic approach to the two appeals, we question the practice that allows, first, the same appeals officer to be used on both cases, particularly since his decisions on the first appeal are being challenged and second, only cost issues not raised in the first appeal to be raised in the second appeal even when new data is available.

In addition to responding to the request questions, our report also questioned the appeals team's reduction of one-time conversion costs by about \$1 million for 40 employees. This issue is very confusing, but it is our understanding that the 40 employees consist of 9 employees which the appeals team said would be RIFed and 31 employees that would be downgraded even if the functions were not contracted out. Therefore, the appeals team position is that the cost of the 9 employees and the cost associated with maintaining the 31 employees in downgraded positions should not be considered in the one-time conversion cost. It appears that the appeals team in its computation did not recognize that the one-time conversion cost associated with the 31 employees related to RIF costs if the functions are contracted out, not to the cost related to maintaining the employees in downgraded positions. Had the appeals team recognized RIF costs, the reduction would have been substantially less than \$1 million.

In addition, the appeals team adjusted the cost comparison to include the cost of three general and administrative positions which added about \$130,000 to the in-house cost estimate. NWC says that contracting out the targeted functions will not be added to the in-house costs. Based on information provided during our review, we believe NWC's position is reasonable.

We have not yet received Navy's response to our report, but it is my understanding that a detailed response is forthcoming.

Mr. Chairman, we will submit a copy of our report for the record.¹

This concludes my statement and I will be happy to respond to any questions you may have at this time.

Senator STEVENS. Well, Senator Cranston and Senator Hayakawa want me to ask some questions of you in particular.

As you examine the Navy policy, have you determined if the Navy followed its own policy?

Mr. GILROY. We have found that, basically, the Navy has followed the policy that was in place. We have had some questions about the guidelines. Our people who did the work at China Lake believe the initial study was rather, or I should say some of the work was rather shoddy. However, the China Lake people were following guidance coming down from Navy—if this is your reference, sir.

Senator STEVENS. Does GAO agree with the Navy's methods to determine the RIF cost?

Mr. GILROY. No.

Senator STEVENS. You heard them explain here—I assume you were in the room. Do you agree with the methods they use to determine the RIF costs?

Mr. GILROY. We attempted to clarify in our statement the confusion that surrounds the RIF cost. When we talk about 40 people, 9 RIFed and 31 downgraded, we still see that the Navy has not considered the RIF cost for these 31 people, as I understood what the Navy said. They talked about downgrading and possibly placing these people. We are talking about going from 40 to 0, if you contract out, and we think these RIF costs should be considered.

Senator STEVENS. You heard the implication that there may be—let me back up here.

The implication here this morning is that there is a possible liability on the part of the Government if the Government does not now go ahead with the contract to Pan Am, notwithstanding the questions about the equity of this appeal. Has there been any case in the past where the Government has been found liable for delay in awarding a contract while it reviewed an appeal of this type?

Mr. GILROY. I am afraid I could not respond to that at this time, Mr. Chairman. I will submit the question to our Office of General Counsel and request a legal opinion.

Senator STEVENS. Well, it is my understanding that this is one of the reasons the Navy says it must go ahead now and not respond to the requests of the Senators from California, because of potential liability to Pan Am if it does not award the contract as it indicated it would do under its interpretation in the original request for a proposal.

We would like to have an answer to that if it is possible.

¹ See p. 25.

Mr. GILROY. Certainly, I will submit it to our Office of General Council and provide an answer for the record.
[The information follows:]

U.S. GENERAL ACCOUNTING OFFICE,
Washington, D.C., January 26, 1983.

HON. TED STEVENS,
Chairman, Subcommittee on Civil Service, Post Office, and General Services,
Committee on Governmental Affairs, U.S. Senate.

DEAR SENATOR STEVENS: During my testimony before your Subcommittee on December 13, 1982, you requested that we advise you as to whether the Government is liable for damages to a low bidder resulting from a delay in the award of a contract. Our Office of General Counsel has determined that the Government would not be liable for such damages.

Sincerely yours,

ROBERT M. GILROY,
Senior Associate Director.

GENERAL ACCOUNTING OFFICE,
January 18, 1983.

To: Senior Associate Director, PLRD/GP—Robert M. Gilroy.
Subject: Government's Liability and/or Potential Liability in Contracting-Out Situations—B-209739

This responds to your December 15, 1982 request for our opinion as to whether the Government would be liable for damages to the low bidder resulting from a delay in the award of a contract pursuant to a solicitation which was issued as part of a cost comparison under OMB Circular A-76. The delays resulted from congressional inquiries into the procurement. We do not believe the Government would be liable for such damages.

You indicate that the agency's initial evaluation indicated that it would be cheaper to perform the required maintenance, warehousing and vehicle operations functions in-house. The low bidder, however, appealed alleging deficiencies in the in-house cost estimate. The agency reversed its initial evaluation and determined that it would be less expensive to contract out the function to the low bidder. This determination was appealed by the affected employees, but the agency affirmed its decision to procure the services from the low bidder. During and since the appeals the agency has received numerous congressional inquiries and the award has been delayed several times while the agency considered those inquiries.

There appears to exist no basis for recovery by a low bidder of damages resulting from a delay by the Government in awarding a contract. Where it is shown that the Government acted arbitrarily or capriciously with respect to a bid or proposal, and because of that action the bidder or offeror was denied the award, the bidder may recover bid or proposal preparation costs. *See Keco Industries, Inc. v. United States*, 428 F.2d 1233 (Ct. Cl. 1970); *Hub Testing Laboratories—Claim for Costs*, B-199368.3, June 18, 1982, 82-1 CPD 602. Since here it appears that the low bidder has or ultimately will receive the contract award, there is no basis for a claim for bid preparation costs.

Futhermore, we do not believe a successful bidder, after award, is entitled to a contract price adjustment on the basis that the award was unduly delayed and, for example, the cost of performance increased as a result. Acceptance of the bid would be predicated on the existence of a viable bid. If, after the initial bid acceptance period, the bidder extends the bid so that it is available for acceptance even after a long delay, the bidder has agreed thereby to perform the contract at the bid price if the bid is accepted at any time during the extended period.

HARRY R. VAN CLEVE,
Acting General Counsel.

Senator STEVENS. I have been sitting on this curbstone as a lawyer for a long time, but I certainly cannot understand how we can have a liability before the contract is signed as long as the review is going on.

In your opinion, can you tell me, did the Navy deviate from your recommendations regarding the appeal procedure? This is Senator Cranston's last question, and it implies you made some specific recommendations concerning the appeal procedures.

Did you make recommendations to the Navy?

Mr. GILROY. Well, our review was after the fact, Senator. I don't know if—let me say that we have commented in our report on the appeals procedure right along the lines that I mentioned in my statement—

Senator STEVENS. One of those things, as I understand it, is that you, too, find it strange the appeal from the decision was made by the appeals officer in the first instance, going back to the same appeals officer. You did comment on that procedure, did you not?

Mr. GILROY. Yes, sir, in our report and I again referred to it in the statement. Allow me to read the passage from the report:

We also recommend the Secretary revise the policies and procedures used in handling second appeals to require a different appeals officer be appointed, and second, allow elements in the first appeal be reviewed again when new data is presented.

Senator STEVENS. Have they responded to that request?

Mr. GILROY. We have not received an official Naval response to that, Mr. Chairman.

Senator STEVENS. Very well. We thank you very much. We thank you, gentlemen, for being here. I appreciate your courtesy in coming on such short notice.

Mr. GILROY. Our pleasure, sir.

[The GAO report referred to in Mr. Gilroy's testimony follows:]

U.S. GENERAL ACCOUNTING OFFICE,
PROCUREMENT, LOGISTICS, AND READINESS DIVISION,
Washington, D.C., November 12, 1982.

Hon. ALAN CRANSTON,

U.S. Senate

Hon. PAUL S. SARBANES,

U.S. Senate

Subject: Navy Procedures Used In Awarding Solicitation No. 62474-82-R-0051 at the Naval Weapons Center, China Lake, California (GAO/PLRD-83-15)

In your September 27, 1982, letter, you asked us to review certain Navy procedures used to award solicitation No. 62474-82-R-0051. The contract resulting from the solicitation will affect family housing maintenance, supply operations and warehousing, and vehicle operations and maintenance functions now being performed by Federal civilian personnel at the Naval Weapons Center (NWC), China Lake, California. Your letter expressed concern that the Navy initially decided it would cost almost \$3 million less to perform these functions in-house rather than by contract as subsequently decided. You asked us to respond to specific questions in your letter before the contract is awarded. On November 8, 1982, we sent a letter to the Secretary of the Navy recommending that he defer the award of the contract until our report has been received and reviewed.

BACKGROUND

NWC prepared its cost estimate to perform the support services in-house and had the estimate reviewed and certified by the Naval Audit Service. Bids were opened on June 29, 1982. NWC announced that based on a cost comparison the in-house cost to perform family housing maintenance, supply operations and warehousing, and vehicle operations and maintenance functions was about \$2.8 million less than the cost of contracting. Pan Am World Services, Inc., the low bidder, filed an appeal in July 1982, alleging deficiencies with the NWC in-house cost estimate. An appeals officer from the Naval Material Command (NAVMAT) in Washington, D.C., was appointed to review the appeal. A review team was established to assist the appeals officer.

In August 1982 the appeals officer concluded that after adjustments, which he had applied, the cost of contracting was \$364,000 less than the in-house estimate. Consequently, the decision to perform the activities in-house was

reversed and the functions were to be contracted. In September, about 400 appeals from NWC employees and others, such as union and civic leaders in the China Lake area, were submitted claiming errors in the adjustments that showed contracting to be less costly. The same appeals officer was selected to evaluate the appeals, and on October 29, 1982, he decided to sustain his decision in favor of contracting for the services at NWC. The contract is expected to be awarded to Pan Am around November 15, 1982.

SCOPE AND METHODOLOGY

We evaluated the appeals officer's adjustments and discussed them with the appeals officer and officials of NWC and NAVMAT. Because of time constraints, we concentrated on areas where Pan Am suggested and where the appeals officer made large adjustments—one-time conversion cost, escalation cost, labor cost (hours), and general and administrative expenses. Also, we obtained the views of the Naval Audit Service, Western Region, San Diego, California, and the Naval Audit Service Headquarters, Washington, D.C., concerning the differences. In addition, we discussed the cost comparison and the adjustments with the leaders of unions representing NWC employees. We also discussed certain adjustments with officials of the Office of Management and Budget's (OMB's) Office of Federal Procurement Policy in Washington, D.C.

It should be emphasized that, because of the short time frame to perform the review, our findings and conclusions are based on our best judgment relevant to the data reviewed and the discussions held.

FINDINGS AND CONCLUSIONS

Questions raised in request

In response to your specific questions, we found the following:

Why did the Naval Audit Service not find discrepancies in NWC's cost estimate? Because of time limitations we were not able to examine this question fully. The auditors' review was concerned with mathematical accuracy and ensuring that NWC followed established procedures in preparing the in-house cost estimate. However, most of the items in question in the adjustments reflected differences in judgment and interpretation of policies by NWC and the appeals officer. Hence, it is doubtful the items questioned would normally be identified during the auditors' evaluation.

Why did the Navy review team not consult with Naval personnel experts? A member of the appeals review team said the team did not feel it was necessary to have personnel expertise because the team accepted the personnel rates NWC used. The team member said the team was only concerned about the number of hours and the number of people involved which, in their opinion, did not require an evaluation by personnel experts.

How was reduction-in-force (RIF) that would result from contracting out projected? NWC projected, as part of its one-time conversion cost, a "mock RIF." The mock RIF was used to estimate the cost to RIF Federal employees if the functions are contracted. The mock RIF was based on the number of personnel needed for the most efficient organization and assumed that all employees would be either RIFed or retired. (The policy on contracting out under OMB Circular A-76 and Public Law 96-342 require an activity considering contracting to base its in-house cost estimate on the most efficient and effective organization). The appeals officer adjusted this projection to correct what he considered to be a "worst case" projection. NWC's management agreed that it should have used some other assumptions, but disagreed with the extent of the appeals officer's adjustments. NWC agreed, for example, that it should have planned on some people going to work for the contractor. We agree that NWC should not have used the worst case projection.

Why did NAVMAT change the figures used to compute labor hours? Based on Pan Am's appeal, the appeals officer calculated the labor hours required for in-house performance by counting the actual workdays in the 3-year contract period to arrive at 2,088, 2,096, and 2,088 hours per year or 6,272 hours total. NWC used 2,080 hours per staff-year (6,240 hours for 3 years) the standard work-year hours used Government-wide and specified in the cost comparison handbook. The appeals officer's calculation increased the in-house cost by adding the cost of these additional 32 hours to each employee included in the in-house

estimate. Using the hourly rates in NWC's estimate, this added about \$53,700 to the in-house cost. We believe the appeals officer's adjustment was more accurate because actual workdays were used.

What are the reasons for the changes in the appeals rules prohibiting a contractor from appealing elements of the study reviewed in the first appeal? The appeals rules were not changed to prohibit only the contractor from appealing those elements of a cost study reviewed in a first appeal. The appeals rules were changed to prohibit any party from appealing any elements reviewed in a first appeal. Before June 30, 1982, the Navy's Commercial Activities Program appeals procedures allowed only one opportunity to appeal. The decision of the appeals officer was final. On July 1, 1982, the appeals procedures were amended to allow appeals that were reversed during the initial appeals process to be appealed. The right of appeal, however, was limited to questions concerning elements that were not considered during the first appeal.

What procedures were used in the appeals process? While it appears that NAVMAT followed the appeals procedures in its basic approach to the two appeals, there are some questionable aspects to the process that was used. For the first appeal, a review team headed by an appeals officer was appointed. The appeal officer was at an organizationally higher level than that of the official approving the initial decision to perform the work in-house, Commander, NWC. The team was assisted in its review at NWC by representatives from other NWC activities, and the Naval Audit Service reviewed the adjustments. The same appeals officer from the first appeal was responsible for reviewing the second appeal. Although there is no specific guidance on how second appeals should be handled, we question the practice that (1) the same appeals officer be used, particularly where, as in this case, his decisions are being challenged, and (2) elements in a first appeal are not appealable in a second appeal, especially when new data is introduced.

Questionable adjustments

Cost of organizing to reach the most efficient organization.—In order for NWC to reach its most efficient organizational staffing level of 207 employees, the appeals officer said 40 NWC employees would have to be retrained, placed in other positions, etc. The appeals officer determined that the cost of repositioning these 40 employees should have been included in the in-house estimate. Since the one-time cost of repositioning these employees was not included in the in-house estimate, the appeals officer reduced the contractor's bid by about \$1 million (the estimated cost to reposition 40 employees).

NWC objected to most of the appeal officer's \$1 million adjustment on the basis that it was contrary to Navy instructions and OMB Circular A-76. NWC states that the instructions specify that the cost comparison should be between the in-house estimate (based on the most efficient organization) and the contractor's bid (including one-time conversion cost). We asked officials of OMB's Office of Federal Procurement Policy about the intent of OMB Circular A-76 in regard to the cost to reorganize to fit the most efficient organization in the cost comparison. These officials said the reorganization cost should not play any part in the cost comparison, that is, the cost should not be added or deducted, and the cost comparison should be against the mock RIF for the most efficient organization. The Office of Federal Procurement Policy officials did not know of any instances where any other agency had treated the cost of reorganizing to meet its most efficient organization in the manner it was treated by NAVMAT. We see no basis for the \$1 million adjustment made for NWC reorganization costs because (1) reorganization costs associated with making an activity more efficient is a normal cost of Government and (2) reorganization costs would not be incurred if an activity is contracted.

General and administrative expenses.—The appeals officer adjusted the cost comparison to eliminate three general and administrative positions, which added about \$130,000 to the in-house cost estimate. While it was not determined where the losses would occur, it was assumed that the loss of about 200 employees by contracting would eliminate the need for three general and administrative employees. However, NWC says that this will not occur and that, at most, it might reduce some overtime. NWC also pointed out that its general and administrative people are currently running parallel payroll systems for a demonstration project, which has placed an extra burden on these people.

RECOMMENDATIONS

As discussed above, we believe there are serious questions that still need to be resolved. Because the cost margin between contracting or in-house performance is small and the decision is of tremendous importance to those parties affected, we believe careful consideration should be given to the issues raised. Therefore, we recommend that the Secretary of the Navy defer award of the contract for support services until the cost comparison has been thoroughly reevaluated. We also recommend that the Secretary revise the policy and procedures used in handling second appeals to (1) require that a different appeals officer be appointed and (2) allow elements in a first appeal to be reviewed again when new data is presented.

We are sending copies of this report to the Secretaries of Defense and the Navy; the Director, Office of Management and Budget; the Administrator, Office of Federal Procurement Policy; the Chairmen, Senate and House Committees on Appropriations and on Armed Services, Senate Committee on Governmental Affairs, and House Committee on Government Operations. We will also make copies available to others upon request.

DONALD J. HORAN,
Director.

Senator STEVENS. Again, on behalf of the Senators and Congressman from California, and this committee, we do request Navy to respond to the suggestion and delay the awarding of this contract until there has been an opportunity for this matter to be appealed to another appeals officer.

Thank you very much.

We will put that in writing if you wish, Mr. Cox, but I think it is implicit in the letter I sent and also in letters from Senators Haya-kawa and Cranston and Congressman Thomas.

We now have a panel of Mr. Lewie Carr, president of local 442, of the International Association of Machinists and Aerospace Workers; Bruce Bonbright, Supervisor of Management Division, Naval Weapons Center; and Dennis Rowell and Les Saxton, Federal Managers' Association.

Mr. Rowell.

TESTIMONY OF DENNIS ROWELL, PRESIDENT, FEDERAL MANAGERS' ASSOCIATION—CHAPTER 28, ACCOMPANIED BY LES SAXTON, MEMBER, FEDERAL MANAGERS' ASSOCIATION—CHAPTER 28, NAVAL WEAPONS CENTER; BRUCE BONBRIGHT, SUPERVISOR OF MANAGEMENT DIVISION, NAVAL WEAPONS CENTER; AND LEWIE W. CARR, PRESIDENT, LOCAL 442, INTERNATIONAL ASSOCIATION OF MACHINISTS AND AEROSPACE WORKERS

Mr. ROWELL. Mr. Chairman, my name is Dennis Rowell. I am president of chapter 28 of the Federal Managers' Association.

The FMA is an organization composed of managers and supervisors in the Federal Government. One of its principal objectives is to ensure that the Government operates in the most cost-effective manner possible.

In keeping with this objective, the FMA supports the policy of OMB Circular A-76 that "The American people deserve and expect the most economical performance * * *" of work. Chapter 28 has 130 members employed by the Naval Weapons Center, China Lake, Calif. Eleven chapter members will be displaced by the proposed contracting action being discussed today.

I want to thank you, Senator Stevens, for holding this hearing on a very critical issue for both civil service employees and for cost-conscious American taxpayers.

I have brought with me my colleague, Mr. Les Saxton, who is also a member of the Federal Managers' Association at NWC. Mr. Saxton is a management analyst and has extensively studied the initial NWC decision, the contractor appeal, and the first and second appeal decisions by the appeal officer. Neither Mr. Saxton nor myself will be directly affected by the outcome of this matter; however, we have traveled here today at FMA expense and are presently on annual leave to share with you our views on the injustices of the administrative appeal procedures in the contracting out process. Also joining us this morning we have Mr. Bruce Bonbright, who is representing the Naval Weapons Center at its request. Mr. Bonbright is familiar with the technical aspects of the initial cost comparison and the appeal official's adjustments in the first and second appeal decisions.

Please allow me, Mr. Chairman, to briefly summarize the appeal procedures, as I understand them. Under OMB Circular A-76 guidelines, after the bid opening all bidders had up to 30 days in which to file an appeal. Pan Am World Services, Inc., whose bid was \$2.8 million above the in-house bid, filed an appeal. Major facets of the administrative appeal procedures at that time called for:

One, appointment of an independent appeal official with no previous involvement in development of the cost comparison.

Two, 30 days for review of the appeal.

Three, no appeal of Government organization or staffing decisions.

Four, the decision of the appeal official to be final.

Subsequently, these procedures were modified to allow a second appeal subject to the conditions that no items reviewed in the first appeal could be questioned and that the same official would judge the second appeal.

Pan Am challenged virtually every cost item within the cost comparison in its appeal to the NAVMAT appeal official. This effectively prohibited a second appeal as to the rationale, methodology or logic used by the appeal official in making his decision. The appeal official ruled in favor of Pan Am on almost all areas with significant dollar impact resulting in the appeal being upheld and the original decision to retain the work in-house being reversed.

This was accomplished by an adjustment of over \$3 million in the cost comparison prepared by the Naval Weapons Center in-house bid team. While I will state that the original cost comparison may have been aggressive toward retaining the work in-house, the cost comparison as adjusted by the appeal official was, in my opinion and in the opinion of some analysts having a much better understanding of the entire process than I, biased toward contracting out to an even greater degree.

The frustration of not being able to present any additional information or to counter the appeal official's ruling through official channels led Mr. Saxton and myself to come to Washington in early September to solicit congressional assistance in support of obtaining a truly independent review. We were successful in bringing about a GAO review and putting a temporary hold on the contract award pending the review. It was our hope that in the process, the Navy

would recalculate certain areas of the cost comparison, this time applying the guidelines correctly. This never came about. The GAO review pointed out that over \$1 million of adjustments made by the appeal official "raised serious questions." The Navy dismissed the GAO report by stating: "The GAO conclusions relating to RIF costs apparently resulted from a misunderstanding by GAO that the original NWC RIF analysis was already based on the MEO, which is incorrect."

This statement by the Navy is true; however, what the Navy failed to disclose was that their analysis was not based on the most efficient organization (MEO) either.

The NWC analysis started from a point four personnel positions above the MEO while the Navy started 12 positions below the MEO and, in their analysis, the Navy further reduced the RIF cost by deleting 40 more positions as common costs.

To this day, the Navy had failed to perform the RIF cost analysis in accordance with existing guidelines. The estimated RIF cost derived from using an actual list of personnel to be affected current as of October 22 and employing the same assumptions and methodology used by the appeal official reflects a high RIF cost estimate of \$1,971,000 and a low estimate of \$1,268,000. The Navy estimate of these same costs is \$676,000.

We believe that with a fair appeal process, this and other cost issues would have been fully examined and the American taxpayer would have benefited by a decision to perform the work at the lowest possible cost.

The cost comparison process is very complex. In this instance, several significant procedural modifications in calculating costs were made during the appeal review. Employees of the Naval Weapons Center who questioned these procedural changes under the revised appeal guidelines were told that the appeal official's judgment had been rendered and was not subject to further appeal.

I might add that we feel uncomfortable in speaking out against Navy decisions since we support the Navy and feel that, on the whole, the Department of the Navy makes good management decisions and supports its employees. However, we feel we must speak out on this issue, both for the good of all civil service employees and because of our desire to see that the Government obtains its services at the lowest possible cost. This concludes my prepared remarks. We will do our best to answer any questions you may have.

Senator STEVENS. I assume that the productivity of these people has been affected during this period.

Mr. ROWELL. Yes, sir.

Senator STEVENS. Have there been any voluntary resignations in this unit during this period?

Mr. ROWELL. Yes, there have.

Senator STEVENS. Have you determined the actual RIF costs for this unit?

Mr. SAXTON. We have reviewed the actual numbers that are currently scheduled to be RIFed, that is, 155 actual separations, 104 changes to lower grade, 30 reassignments without change in pay.

In addition, there will be approximately 100 temporary employees discharged prior to the award of the contract.

My personal estimate of the cost associated with this RIF is \$1.4 million. That was calculated yesterday.

We have with us Mr. Bonbright, who has prepared a cost estimate, I believe, in late October, that gives a range of costs associated with the RIF; maybe he could give us those numbers now.

Senator STEVENS. Mr. Bonbright?

Mr. BONBRIGHT. Yes, Senator Stevens.

First I want to point out the numbers I am going to give you are the numbers that may not be actual, they are just a range of numbers that occur. We won't know what the actual RIF costs will be for probably 3 years.

With that caveat in mind, we estimate it could range somewhere between \$1,200,000 and \$1,900,000, but I would like to point out a couple of important factors.

We have no way of knowing how many of our employees will next accept employment with the contractor. Which employee does may make a substantial difference in the RIF cost. We don't know how many people will elect to go and take a voluntary retirement instead of taking a change of lower grade. We are not sure how many vacancies will occur over the next 90 days if we have the 90-day notification.

These factors are fairly important in terms of the ultimate RIF costs and so the actual RIF costs could range extensively, and it could be a lot lower than I gave because of the fact that the employees may take employment with the contractors.

So I want to put that caveat there. It is very difficult to give you any kind of a precise dollar amount.

Senator STEVENS. Has the appeals officer been given these cost figures that you have given us?

Mr. BONBRIGHT. Yes, sir, and again these are starting numbers and the appeals officer would then have to determine in his mind how many employees did in fact work for the contractor, reasonable estimates of these factors.

Senator STEVENS. Somewhere along the line, Mr. Carr, I assume that employee organizations questioned these RIF costs. When was that?

Mr. CARR. As soon as the reversal was made, we got notification; we didn't have it in writing. So we sat down and prepared a written appeal addressing the issue that at the time we were notified we did not have a notification that we could not appeal the things that were appealed before. We went ahead and prepared a statement to go back, because we had the actual figures. I calculated them more than half a dozen times, and it showed that adjustment that the reviewing officer made was completely out of line.

If you were to take your mock RIF, for instance—I maintain that NWC was wrong to begin with—I took it from 203 positions to 0, which OMB should have and does recommend, and it comes out substantially higher.

I want to point out one difference here that only 60 percent of that one-time conversion cost is even chargeable to the contractor, so he automatically has a 40-percent advantage. He does not get charged 100 percent of the RIF cost, but 60 percent of it.

Then they come up and penalize us again by another 40 positions.

You asked before if you thought the contractor had an advantage. Yes, he definitely does.

Senator STEVENS. Now, who made the original decision that Pan Am appeal? I assume that it was someone at China Lake.

Mr. CARR. That they did what?

Senator STEVENS. The original decision that the contracting out was not in the best interest of the Government; who made that?

Mr. ROWELL. NAVMAT.

Senator STEVENS. But who made the first decision out there that Pan Am was wrong?

Mr. ROWELL. Naval Weapons Center.

Senator STEVENS. Do you know specifically what unit, where that decision was made?

Mr. ROWELL. I believe it was the CA review team.

Senator STEVENS. Then when Pan Am wanted to review that decision, they went to the appeals officer.

Mr. ROWELL. That is correct.

Senator STEVENS. Then when you appealed for the employees, Mr. Carr, your appeal was directed to the same appeals officer?

Mr. CARR. Yes, it was.

Senator STEVENS. Did your people ask for a different appeals officer?

Mr. CARR. Yes.

Senator STEVENS. When did you do that?

Mr. CARR. When we turned it in in writing we asked for a different review officer before the deadlines of appeals.

Senator STEVENS. Did you get a response for that specific request?

Mr. CARR. No, sir, we did not.

Senator STEVENS. How many employees are there in this unit now?

Mr. SAXTON. There are currently 155 employees scheduled for separation, that is, who received initial notice.

We have done many of the things that were earlier alluded to as being good management practices by placing people in other organizations and trying to maintain jobs in other positions for as many as we could.

We have reduced the number of people that will be initially affected from the level of 191 that existed on August 1, down currently to 155 separated.

Now that means that there are a total of about 389 people that will be impacted, but only 155 separated.

Senator STEVENS. Explain who those other people are.

Mr. SAXTON. Individuals that are going to be affected by the bump and retreat rights of those directly impacted.

Senator STEVENS. What about these temporary employees?

Mr. SAXTON. They have no retention rights per se. They are employed at the pleasure of the Government and can be terminated immediately.

Senator STEVENS. They are not involved in the 155?

Mr. SAXTON. No, they are not.

Let me add here, in calculating RIF costs, I made an assumption that 45 percent of the 155 individuals being displaced would be employed by Pan Am, and my costs are based on that assumption. They are also pro rated to reduce the total cost by 40 percent to conform with the A-76 guidelines.

Senator STEVENS. You are part of the Federal Managers' Association.

Mr. SAXTON. Yes, sir.

Senator STEVENS. Even with that assumption of 45 percent you found the contracting out was not in the best interest of the Government?

Mr. SAXTON. That is what I have done.

Senator STEVENS. Of the 155, how many are members of the Federal Managers' Association?

Mr. SAXTON. We have 10 members who will be directly impacted, and there are others that are either spouses or friends. It is a small community.

Senator STEVENS. How many of these people are members of your union, Mr. Carr?

Mr. CARR. They comprise about 50 percent of the total dues-paying membership in my local.

Senator STEVENS. Are any other unions involved here?

Mr. CARR. Yes; there were appeals filed by the Carpenters International, the Electricians International, Plumbers and Painters International.

Senator STEVENS. Is Pan Am an organized union company?

Mr. CARR. No, sir.

What happened in our appeal, we believe the appeal officer should have gone on the most current Pan Am hiring practice that happened in July, instead of using 45 percent 2 years ago.

What happened, Pan Am came into an organized group, the janitorial, where there were 130 employees employed. Out of that 130, they retained 28, and laid off 102.

Now I have no reason but to believe that is going to happen to organized labor there, and therefore should have been 22 percent, not 45, that they based it on. They would not listen to us at all.

Senator STEVENS. Again I don't have any further questions of you gentlemen. It is possible that the Senators from California may ask some specific questions.

[The prepared statement of the Federal Managers' Association follows:]

PREPARED STATEMENT OF THE FEDERAL MANAGERS' ASSOCIATION

Mr. Chairman, the Federal Managers' Association is a voluntary membership organization of managers and supervisors of all levels of government. Our membership includes both wage grade supervisors and General Schedule managers. Total membership exceeds 16,000 members distributed among more than 200 chapters.

One of those chapters is #28 at China Lake, California, whose President Dennis Rowell will present these comments for the record.

Before discussing the specific contract issue before this Committee today, it would be useful to the members of the Committee to understand the general view of FMA toward contracting-out. The perspective of FMA is from our members who are managers in hundreds of local government facilities. Their concern revolves around these basic questions: 1. Is the work necessary? 2. Will contracting the work to a private sector firm or doing it in house be the most efficient means of accomplishing the specific work? 3. Which of the two options will be the most cost effective? 4. What are the long run consequences of the two options? 5. Which of the two options best insure the level of quality performance that is necessary?

Mr. Chairman, these are the bottom line questions in good management of funds and human resources to accomplish a work function. Whether in private business or government, they must be answered objectively by the people who bear the responsibility for the decision.

The system which provides for a review of a contract decision must be designed to answer those questions because the decision must be free from extraneous political issues such as personnel ceilings. Clearly, that was, is and certainly should be the intent of Circular A-76 which governs the contracting-out process.

It is the contention of FMA that the decision to contract-out housing maintenance, transportation and supply services at China Lake Naval Weapons Center was and is contrary to the aforementioned principals. More specifically, the appeal process appears to have been used as a deliberate means of altering an earlier decision and shutting off any further review even though questionable changes were made in the in-house bid. These changes and alterations in the cost analyses caused a swing of more than 3.2 million dollars in favor of the contract. While it is conceivable in the complexity of cost analysis that some variances might be found, a swing of 20% of the total bid raises serious doubts as to the quality of the appeal review. Raising even more doubt is the fact that the Navy Audit Service which has no preference either way found few discrepancies in the original bids.

Mr. Chairman, the appeal process must be designed to insure that the management principals alluded to earlier are maintained. This is not the case at present. Our Association has had to intercede many times when managers' careers were threatened because they tried to appeal a decision to contract. Not three months ago FMA appealed a contract decision at an Army installation because a manager was warned that his future was in jeopardy. The appeal was upheld and the work stayed in house. It is interesting to note that it was the second time the function was reviewed for contracting in two years. We learned last week that it will be reviewed again in the next few months. You can imagine the morale of the Federal employees whose jobs are constantly threatened.

The Federal Managers' Association is very proud of the courageous efforts of the managers at China Lake who are here today. They represent the finest we have in Government, spending their own money to come here today in behalf of the highest and best use of the taxpayers dollars and our human resources. They can discuss the China Lake situation in detail and they have the full and complete backing of the FMA.

Senator STEVENS. I do want to be informed before the end of the day whether the Navy intends to delay the awarding of this contract, as has been requested by this committee and by the Senators from California and Congressman Thomas.

Captain Newcomb, could you let us know from your office?

Captain NEWCOMB. Yes, sir.

Senator STEVENS. If there is nothing further to come before this committee, the committee stands in recess. Thank you very much.

[Whereupon, at 9:30 a.m., the subcommittee was recessed to reconvene at the call of the Chair.]